No. 10625

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

ROSE PAPANTONIO, suing in her own behalf as a shareholder of TRANSAMERICA CORPORATION and in behalf of all other shareholders of said corporation similarly situated,

Appellant,

vs.

AMADEO P. GIANNINI, L. M. GIANNINI, A. H. GIANNINI, AMADEO P. GIANNINI (as Executor of the Last Will and Testament of Virgil D. Giannini, Deceased), BANK OF AMERICA NATIONAL TRUST & SAVINGS ASSOCIATION, a national banking association (as Administrator-with-the-Will-Annexed of the Estate of John M. Grant, Deceased), GORDON GRAY, O. D. HAMLIN, T. W. HARRIS, A. P. JACOBS, F. C. STEVENOT, RUSS AVERY, P. A. BRICCA, GEORGE J. DE MARTINI, W. N. LAGOMARSINO, A. J. SCAMPINI, WILLIAM E. BLAUER, LEON BOCQUERAZ, E. H. CLARK, CHARLES N. HAWKINS, W. F. MORRISH, A. J. MOUNT, ALFRED E. SBARBORO, CHESTER H. LOVELAND, P. C. HALE, JAMES A. BACIGALUPI, ARMANDO PEDRINI, GEORGE A. WEBSTER, E. J. NOLAN, C. R. BELL, W. W. GARTHWAITE, GEORGE N. ARMSEY, LOUIS FERRARI, V. SCIALOJA, THEODORE M. STUART, HERBERT E. WHITE, CHARLES DE Y. ELKUS, WILLIAM S. HOELSCHER, CLIFFORD P. HOFFMAN, C. J. SMITH, VERNON C. WALSTON, AMADEO P. GIANNINI, L. M. GIANNINI and CLAIRE GIANNINI HOFFMAN, transacting business as co-partners under the firm name and style of WALSTON & CO., and AMADEO P. GIANNINI (as the Executor of the Last Will and Testament of Virgil D. Giannini, a deceased member of said co-partnership), WALSTON & CO., a co-partnership and TRANSAMERICA CORPORATION, a corporation,

Appellees.

APPELLANT'S REPLY BRIEF

VINCENT A. MARCO,
PERCY V. CLIBBORN,
HOMER N. BOARDMAN,
245A South Beverly Drive, Beverly Hills,
Attorneys for Appellant.

Parker & Company, Law Printers, Los Angeles. Phone TR. 5206.

TOPICAL INDEX.

TABLE OF AUTHORITIES CITED.

CASES. PAGE

PAGE

INDEX TO APPENDIX.

No. 10625

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

ROSE PAPANTONIO, suing in her own behalf as a shareholder of TRANSAMERICA CORPORATION and in behalf of all other shareholders of said corporation similarly situated,

Appellant,

vs.

AMADEO P. GIANNINI, L. M. GIANNINI, A. H. GIANNINI, AMADEO P. GIANNINI (as Executor of the Last Will and Testament of Virgil D. Giannini, Deceased), BANK OF AMERICA NATIONAL TRUST & SAVINGS ASSOCIATION, a national banking association (as Administrator-with-the-Will-Annexed of the Estate of John M. Grant, Deceased), GORDON GRAY, O. D. HAMLIN, T. W. HARRIS, A. P. JACOBS, F. C. STEVENOT, RUSS AVERY, P. A. BRICCA, GEORGE J. DE MARTINI, W. N. LAGOMARSINO, A. J. SCAMPINI, WILLIAM E. BLAUER, LEON BOCQUERAZ, E. H. CLARK, CHARLES N. HAWKINS, W. F. MORRISH, A. J. MOUNT, ALFRED E. SBARBORO, CHESTER H. LOVELAND, P. C. HALE, JAMES A. BACIGALUPI, ARMANDO PEDRINI, GEORGE A. WEBSTER, E. J. NOLAN, C. R. BELL, W. W. GARTHWAITE, GEORGE N. ARMSEY, LOUIS FERRARI, V. SCIALOJA, THEODORE M. STUART, HERBERT E. WHITE, CHARLES DE Y. ELKUS, WILLIAM S. HOELSCHER, CLIFFORD P. HOFFMAN, C. J. SMITH, VERNON C. WALSTON, AMADEO P. GIANNINI, L. M. GIANNINI and CLAIRE GIANNINI HOFFMAN, transacting business as co-partners under the firm name and style of WALSTON & CO., and AMADEO P. GIANNINI (as the Executor of the Last Will and Testament of Virgil D. Giannini, a deceased member of said co-partnership), WALSTON & CO., a co-partnership and TRANSAMERICA CORPORATION, a corporation,

Appellees.

APPELLANT'S REPLY BRIEF

Introductory Remarks

In presenting this brief we have in mind not only the importance of the case to the parties but also the great

Italics ours unless otherwise stated.

necessity of uniformity of decision in the application of the Civil Rules of Procedure.

It will be noted that although the rules of Civil Procedure for the District Courts of the United States were promulgated to reform and make simple, among other procedures, the manner of "pleading" yet some conflict appears in the decisions even in applying these simple rules. In some instances the courts seem reluctant to discard the former theory of pleading with its many technicalities concerning "ultimate facts", "evidentiary facts," and so called "conclusions of law".

The "pleading" which is involved in this case was prepared according to the views expressed in the decisions which, in our opinion, reflect the sound meaning of the reformed practice. We call attention to this point as a large part of appellee's brief is based upon "technicalities" of pleading which we thought removed from that field of procedure.

We have also devoted, in our effort to be helpful, considerable space to a discussion of the doctrine of "laches", as distinguished from the statute of limitations, in cases lying wholly within the exclusive equitable jurisdiction of the court.

It will be noted that many of the decisions, wherein a State statute of limitations is applied in a Federal court, the basis thereof was the Conformity Act, (28 U. S. C. A., Section 724) which limited the application of the statute to common law actions and was not binding upon the Federal Courts in the administration of equity. The fact that the Conformity Act has or may be superceded by the Federal Rules of Civil Procedure would seem to make no change in the administration of the "doctrine of laches" in equitable proceedings.

The point presented by appellees that appellant's pleading is defective because the corporate departments and agencies of the Transamerica Corporation are not made parties to the action is based upon a misapprehension of the appellant's "pleading", and the erroneous assumption that she is seeking to recover on behalf of such instrumentalities. This is not the case.

Permit us to suggest that appellees' brief is filled with matter which seeks to divide appellant's "claim" into parts and destroy each one by one. This is done in face of the fact that appellant's action is one to *judicially establish a trust relationship between the appellees as trustees and the defendant "Transamerica Corporation" and its shareholders as beneficiaries, coupled with an accounting for secret profits and corporate losses.* We have at times characterized our action as one for an accounting but the fact that it is actually one to establish a trust should not be overlooked, especially in considering the appellees' attempt to seggregate it into independent claims in order to destroy it by the misapplication of academic principles of law.

In presenting our closing argument we shall endeavor to give a definite reply to each of the authorities cited and points urged by the appellees except such points and authorities which are obviously without merit or refer to the practice of the court prior to the adoption of the rules of civil procedure.

We submit the following argument and authorities:

Relating to Appellees' "Statement of the Case."

(Appellees' Br. pp. 3-26.)

Appellees refer to appellant's "Statement of the Case" set forth in her opening brief as "definitely inadequate." (Br. p. 3.) We respectfully, but firmly, assert that appellees' "Statement of the Case," in many respects, is an overstatement of irrelevant matter used as a basis for argument beyond the scope of the points involved.

It is our position that certain of the proceedings in this action, relied upon by appellees, have no place in this appeal. *No ruling was made and no order granted* in the hearing upon appellees' motions directed to appellant's first amended complaint.

The statements of the court and the replies of counsel with respect to a "separate statement of claims" were all directed toward the first amended complaint *and the situation as it then existed.* We know of no authority and none is cited by appellees wherein either court or counsel by merely engaging in informal discussion concerning a pleading presently before the court restricts the basic right of a plaintiff, where general permission is granted, to thereafter choose a different legal theory of his client's case based upon facts *subsequently discovered,* and present the same for consideration upon the merits.

It will further be observed that the trial court made no order and gave no direction to the effect that appellant's complaint should be divided into several "statements of claims" *as a condition* for the filing of her second amended complaint.

The statements of the court with respect to such subject and counsel's replies relate solely to the situation as it appeared from the facts *then* disclosed.

This is definitely demonstrated by the minute order entered at the close of the argument on the motions directed to the first amended complaint which is as follows [R. p. 142]:

> "The court makes a statement *re its present views.* It is ordered that the plaintiff serve and file amended complaint within sixty (60) days and that the defendants have thirty (30) days thereafter to plead thereto." (Italics ours.)

The court limited its statement to its *present* views but did not bring the same forward as a condition of the order permitting the amendment. The court reserved the right to change its views. We should have the same right and with like grace we respectfully submit that counsel's statement to the effect that: "We have no objection to separating our complaint into counts * * *" was directed only to an action founded upon the facts as *first* known and presented in appellant's first amended complaint.

It is clear that if appellant had filed a second amended complaint in violation of an order of the court it would have been stricken from the files upon motion of the court or that of the appellees. This did not occur. The appellant's second amended complaint was tested on its merits by appellees' motion to dismiss and other motions, including "A Motion to Separately State Claims" *upon which the trial court made no ruling.* There is not a word nor a sentence within the "Memorandum of conclusions" of the trial court which in any manner indicates that the filing of appellant's second amended complaint was in violation of a court order nor that the appellant's motions to dismiss were granted upon such ground.

We do not feel justified in using our space upon an argument of this character but before passing to another subject we direct the court's attention to the statement made by counsel to the court at the time appellant's second amended complaint came before the court upon appellees' motion to dismiss. Our statement as paraphrased by the trial court is as follows [Appellees' Br., Appendix pp. 13-14]:

> "In justification of this type of pleading plaintiff's counsel, during the oral argument upon the pending motions, asserted *that subsequent to the entry of the order granting leave to file a second amended complaint certain matters had come to their attention which had induced them to adopt a different legal theory respecting this litigation, and it was accordingly upon this new theory that the present complaint had been drawn.* Such different theory, counsel *explained* was to the following effect.
>
> "The first amended complaint was based upon the proposition that two of the defendants and a third person since deceased (whose legal representative was joined as a defendant) had conspired to acquire control of Transamerica and its affairs, that pursuant to such conspiracy, they had selected its directors, dominated its affairs and caused its directors to commit various breaches of their trust or fiduciary obligations and that in furtherance of such conspiracy various overt acts had been committed at the time, in the manner and in the particulars therein pleaded, causing damages to Transamerica in the respective amounts therein alleged. On the other hand, the second amended complaint was prepared upon the theory that all of the persons who at any time had

served as directors of Transamerica had conspired to commit the aforementioned breaches of their trust or fiduciary obligations, that in furtherance of such conspiracy certain overt acts had been committed at the times, in the manner and in the particulars therein pleaded, causing damages to Transamerica, its subsidiaries and departments in the respective amounts therein alleged, and that such of the defendants as had never served as directors were joined upon the theory that they had aided their co-defendants in committing one or more of the alleged breaches of trust.

"It is the contention of plaintiff's counsel that but a single conspiracy has been pleaded in the second amended complaint; that all of those directors and any others who at any time allegedly entered such conspiracy are equally liable regardless when, if at all, they served as directors of Transamerica; also, that it is immaterial when the different alleged overt acts were committed or when damages resulted therefrom; and that even though it may be pleaded that different defendants, acting either as directors or otherwise, entered the alleged conspiracy at different times, nevertheless, according to the allegations of said complaint, they are charged with having adopted the entire, single, illegal scheme, and hence all defendants are equally liable for all wrongs committed, including not only those perpetrated before they became directors or before they otherwise aided the alleged conspiracy, but also for all the various wrongs asserted to have been committed after they had ceased to be directors of Transamerica, or otherwise had terminated their connection with the enterprises claimed to have been involved with said conspiracy."

It will be observed, even from this paraphrased version, that our remarks with respect to the second amended complaint are merely explanatory of the appellant's case *then* before the court *and are not addressed to a claimed violation of any alleged prior order of the court.* They were considered by the court as part of our argument in support of the sufficiency of the pleading. The court, as stated by appellees (Br. p. 23), ruled against appellant's views with respect to separately stating claims. As appellees' motions in that regard were not passed upon, we assigned the court's conclusion as error in this respect. (Op. Br., Point V, specification (1), p. 41; Point VI, specification (1), by reference, p. 41; Point VII, specification (1) by reference, p. 42.)

Our argument with respect to said specifications of error appears as part IV of appellant's Opening Brief, pp. 97-111. We again assert that our general view of appellant's case as paraphrased by the trial court constitutes an accurate statement of the law as applied to appellants' second amended complaint.

The colloquy between court and appellant's counsel was not designated by us as part of the record on appeal and we entertain a definite view that none of the oral argument before the trial court is binding upon this court nor upon counsel and has no relevancy to the sole and only ruling of the court to the effect that the motions to dismiss be granted while all other motions remained undetermined. Under the present circumstances, however, we feel justified in suggesting to the court that, in the event the point here presented by appellees is considered material, appellant should be entitled to amend the record on appeal to show the entire comments of the court and

the complete replies of counsel upon that subject, as the court's paraphrased version thereof does not, in our opinion, fully express the nature and extent of the subject as then treated.

Replying to Appellees' Argument No. I.

(Br. pp. 27-36.)

This appeal presents no issue nor does our opening brief present any argument with respect to appellant suing on behalf of the corporation. Such is the very basis of appellant's action. We have not overlooked this principle. We seek to enforce it.

We see but two things inferred by appellees' argument here discussed, (1) that a different and more strict rule of pleading prevails in a shareholder's "derivative action" where the plaintiff is the owner of a small number of shares than it does in a case where the plaintiff is the owner of a large number and (2) the obvious inference that appellant's action is to cultivate a fertile field in which to grow an exorbitant fee for her attorneys.

We submit that neither argument is valid. The rules of pleading are not discriminatory. They apply alike to all. Pleading is now governed by the "Federal Rules of Procedure" and not by State practice nor former decisions which conflict therewith. (This subject is discussed in our opening brief at pp. 43-68.)

It is true that some of the courts have given some consideration, under the circumstances of a particular case, to the fact that a plaintiff owns but a small amount of the capital stock of the corporation which he seeks to protect. But the rules of pleading are not altered. No case

is cited by appellees nor, to our knowledge, does any case exist wherein a decision *turns* upon such fact. It is only mentioned in conjunction with other *fatal* defects in pleading or proof.

As counsel for appellees have seen fit to infer that appellant's counsel, if successful, will obtain, by court order, an excessive fee we feel justified in directing attention to *judicial recognition* of the difficulties, discouragements and *their causes* which confront minority shareholders in derivative actions and the nature and extent of the work required by attorneys in prosecuting such actions. *This judicial recognition is especially applicable to the appellant in the present action.* We refer to the remarks of Justice Davis in the case of *Dresdner v. Goldman-Sachs Trading Corp.,* 269 N. Y. S. 360, wherein certain motions to dismiss on the ground of "another case pending" were denied. At page 364 of the Opinion, the court states:

> "The absence of direct authority on the question here presented may indicate that for a long period of years the right of *any* stockholder to invoke the aid of the courts in his individual action has gone unchallenged. However, stockholders in large corporations are, *as a matter of common knowledge, generally uninformed,* and in a measure indifferent concerning the management of the corporation. Generally, *without inquiry,* they sign proxies as a matter of course so that directors and officers may be reelected and their policies may be continued. When dividends cease and the stock becomes comparatively worthless, they may complain and grumble, *but rarely will they resort to the courts for a remedy,* The reason for such inertia is readily found. Stock-

holders are widely scattered and have no definite method of contract with each other. *They usually know that the evidence is almost exclusively in the control of those who are charged with delinquency;* that those same individuals are likewise in control of the funds of the corporation and may apply them in defense of their acts, whether those acts are innocent or wrongful; *that in seeking a remedy the stockholder will be met with every obstacle and procedural delay that the ingenuity of skilled counsel can devise,* as is illustrated in the present case; and that the litigation must entail on their part a great expense with the eventual result in doubt. So, unless a group is organized by ambitious counsel, *or one* or more *stockholders have great courage and ample means to maintain a long-continued litigation,* the stockholders remain quiescent, accepting their misfortune as a decree of relentless fate. It is only in times of general cataclysm or great stress, like those of the present, that indignation will flare up into some decisive action. Common experience tells us that, when officers and directors of a wrecked corporation are called to account, they are not eager to go to an early trial on the merits—whatever the merits may be. *There is great reluctance to furnish the evidence of their acts of management and make disclosure of books and records. The way of the inquiring stockholder is beset with difficulties and discouragements created chiefly by those whose acts are attacked.* Such, in brief, is the background of the average stockholder's action as we view it."

It is within such difficulties and hazards assumed by minority shareholder in a derivative action that we, too, o afield of the record to show the nature and extent of

the work required to obtain *precise* information regarding *concealed facts which are wholly within the knowledge of the appellees.*

It is in the light of such a situation that we ask the court to consider and pass upon the form and sufficiency of the allegations contained in appellant's second amended complaint in order that the pleading may be construed as to do substantial justice. (Rule 8(f).)

If, as said by appellees, appellant is the guardian *ad litem* of the "corporation" the corporation is an "incompetent" whose rights should be regarded with at least reasonable liberality.

The facts set forth in appellant's "pleading" are admitted by the motions. They are not altered nor weakened by the number of shares of capital stock held by appellant nor by the amount of the attorney's fees which, in the event of success, may be awarded her attorneys.

In the case of *Dannmeyer v. Coleman,* 11 Fed. 97, cited at page 31 of appellees' brief, the action, under the facts there averred, was held barred by lapse of time upon the ground that the means of knowledge were open to the shareholders more than 3 years prior to the filing of the action and the complaint was wholly insufficient because it failed to show a case for the jurisdiction of the court and also failed to allege an excuse for not making a demand for action by the directors. The decision did not *turn* upon the number of shares of stock held by the plaintiff.

The rule with respect to a "very clear case" mentioned in 4 Thompson Corporations (2d ed.) 1034, Sec. 4566, cited at page 32 of appellees' brief, finds support in a case

where the act *was not ultra vires nor fraudulent* but was one of business judgment.

In the case of *Trimble v. American Sugar Refining Co.,* 61 N. J. Eq., 340, cited by appellees at page 32 of their brief, the acts of the directors for which relief was sought were not *ultra vires,* they constituted a "corporate policy" only as distinguished from *fraudulent* or other *ultra vires* acts. The facts in that case are far apart from those in the present action and the question of pleading there involved is not here presented.

The case of *Wenberger v. Quinn,* 35 N. Y. S. (2d) 567, cited at page 36 of appellees' brief does not involve *ultra vires* or *fraudulent* acts on the part of the managing directors of the corporation but involves only a question of mere business judgment or expediency. The case is not in point, the pleading is entirely different and its deficiencies do not appear in the pleading under discussion.

When carefully analyzed the expression "a very clear case" and "suspicious circumstances" used by the courts in said cases has very little meaning when applied to pleadings. Rules with respect to pleadings are and must be uniform and cannot be tested by the amount of a plaintiff's investment. Such expressions may have some place in cases which have been tried upon their merits and where other fatal deficiencies appear to which they may be applied.

With respect to the subject here discussed regarding the small amount of shares held by the appellant in the defendant corporation we point out that in one of the early important derivative suits, namely *Dodge v. Woolsey,* 59 U. S. 331, decided in December, 1855, the plaintiff was

the owner of but thirty (30) shares of the Commercial Branch Bank of Cleveland, which was a branch of the State Bank of Ohio. It may also be observed that he was successful in the prosecution of the suit which resulted in a permanent injunction against a tax collector which the directors, *in violation of their duties,* refused to prosecute.

We respectfully but firmly urge that appellees' "Argument No. I" is not an effective answer to any portion of appellant's opening brief and especially that portion which discusses the new rules of pleading and the decisions thereunder. (Op. Br. pp. 43-68.)

At page 29 of appellees' brief, the following statement is made:

> "A stockholder has no vested right to represent the corporation. Rather it is a privilege dependent upon procedural statutes or rules."

This statement, which appellees seek to support by the District Court decision in *Perrott v. United States Banking Corporation,* 53 Fed. Sup. 953, 956 and *Klum v. Clinton Trust Co.,* 48 N. Y. S. (2d) 267, 268, is obviously made for the purpose of attempting to avoid the rule of *Erie Railroad Company v. Tompkins,* 304 U. S. 64, by reason of which the substitutive law of the State of Delaware governs this case with respect to the rights of the parties.

In view of the doctrine announced in *Bachus-Brooks v. Northern Pacific Railway Co.* (8th Cir.), 21 Fed. (2d) p. 4, it is clear that appellees' statement to which we have referred is, indeed, erroneous. It entirely ignores the equitable interest which the shareholder has in his

corporation. It fails to comprehend the fact that a shareholders "derivative suit" is a creature of equity established to grant relief for the character of wrongs presented in the present case and which has existed in England and in this country by an unbroken line of decisions long prior to the decisions in *Dodge v. Woolsey,* 59 U. S. 331, wherein it is stated at page 341 as follows:

> "It is now no longer doubted, either in England or the United States, that courts of equity, in both, *have a jurisdiction over corporations, at the instance of* ONE *or more of their members;* to apply preventive remedies by injunction to restrain those who administer them from doing acts *which would amount to a violation of charters, or to prevent any misapplication of their capital or profits,* which might result in lessening the dividends of stockholders, or the value of their shares, as either may be protected by the franchise of a corporation, *if the actions intended to be done created what is in the law denominated a breach of trust.* And the jurisdiction extends to inquire into, and to enjoin, as the case may require that to be done, any proceedings by individuals, in whatever character they may profess to act, if the subject of complaint is an interpreted violation of a corporation franchise, or the denial of a right growing out of it for which there is not an adequate remedy at law. 2 Russ & Mylne Ch. R., Cunliffe v. Manchester and Bolton Canal Company, 480, n; Ware v. Grand Junction Water Company, 2 Russ & Mylne, 470; Bagshaw v. Eastern Counties Railway Company, 7 Hare Ch. R. 114; Angell & Ames, 4th ed. 424, and the other cases there cited."

Rule 23 (b) has nothing to do with the substantive equitable nature of derivative actions. It merely enacts

into a court rule the former decisions of the courts with respect to certain conditions which must exist in order that a shareholder may be qualified to represent the corporation in a suit of that nature but, being qualified, the action involves the complete and full exercise of an equitable right and must, in the present case, be governed by the substitutive law of the State of Delaware. We find nothing in the decisions cited by appellees in support of their said statement which in any manner conflicts with our foregoing observation upon the subject.

At page 33 of appellees' brief the following statement appears:

> "Throughout her brief appellant has overlooked these principles. She treats the case as if she were the owner of the alleged cause of action as if she were here suing to enforce her individual rights."

It is perhaps unnecessary to answer the foregoing statement as the prayer of appellant's pleading and the plain and simple averments thereof constitute a complete reply.

In a footnote at page 33 of appellees' brief, the case of *D. E. Loach v. Crowleys Inc.*, 128 Fed. (2d) 378, 380 is cited in an attempt to support certain remarks of the trial court in its "memorandum of conclusions," concerning which we make comment at pages 66 and 67 of our opening brief. Appellees', in their footnote, in stating that in making the remarks in question the trial court apparently had in mind the principal laid down in the *Loach v. Crowleys Inc.* with respect to expensive trials of meritless claims which may be avoided by pre-trial and summary judgment procedures, fails to point out that appellant's case is not before the court upon pre-trial or

summary judgment procedure. Counsel for appellees fail to recognize that the point presented by the appeal is the sufficiency or insufficiency of appellant's pleading the admitted allegations of which do not disclose a meritless claim but on the other hand show an enormous wrong. We still feel that our comment with respect to the trial court's observations in question, mentioned at pages 64, 65, 66 and 67 of our opening brief are proper and have a rightful place in showing the error of the trial court in its ruling and judgment given herein.

Appellant's Reply to Appellees' Argument No. II.

(Brief pp. 37-58.)

That part of appellees' argument which attempts to indicate that appellant, in filing her second amended complaint, violated an order of the trial court is, as heretofore shown, unfounded. It is discussed by us only because of appellees' attempt to create such an order by an unwarranted interpretation of a colloquy between court and counsel. We again assert that the statement made by counsel for appellant to the court during informal discussion in question (Br. p. 13) that he had "no objection to separating our complaint into counts on the various statements of the claims" referred only to the appellants' action as then expressed in her first amended complaint and did not contemplate *subsequent discoveries of facts* which fully justify the allegations of the second amended complaint. Counsel's full duty toward his client which requires him to submit her case upon *all the facts* upon which he is informed and adopt a legal theory of recovery based thereon *exists at all times* and cannot be so easily cast aside as appellees have attempted to persuade

the court to do. The trial court did not consider that an order was violated by appellant in filing the second amended complaint. The motions to dismiss were heard and determined *upon the merits of that complaint.* The court did not attempt to obstruct the full rights of the appellant to state her case upon and according to her own theory and upon all the facts which were available to her. To the effect that a litigant has such right which cannot be erased, at least by unwarranted inference, needs no authority for support.

At page 39 of appellees' brief, the case of *Lofland v. Cahall,* 13 Del. Ch. 384 is cited to the effect that officers and directors of the corporation are held to a fiduciary standard applicable to *trustees* and for some purposes will be treated as trustees for the stockholders collectively "which is only another way of saying that they are trustees for the corporation." We agree to this principle of the Delaware law and urge its full and complete application upon all phases of appellant's case. From this doctrine it must be held that the right of action of the corporation against its managing directors *as sought to be enforced by appellant as a shareholder* can only be one for an accounting irrespective of the nature and extent of the items involved, as they were all parts of one general enterprise and sprang from *one* series of operations which by their very nature require an accounting, and consist of but a single cause of action.

Kilbourn v. Sunderland, 130 U. S. 505, cited at page 102 of our Opening Brief, is a complete answer to appellees' argument concerning "separate statements of claims." This decision is quite sufficient to reverse the trial court upon this part of its ruling. Appellees' answer

to this citation, found at page 45 of their brief, evades its effect.

The case of *Cwerdinski v. Bent,* 11 N. Y. S. 208, cited at page 39 of appellees' brief, is not in point. The statement of the court, relied upon by appellees, to the effect that the corporation could have brought an action at law for money had and received was merely hypothetical *for the purpose of applying the Statute of Limitations* upon the theory that the shareholder had no greater right than the corporation. The case involves no factual complexity requiring an accounting. The decision does not hold that the shareholder's derivative suit for an accounting was in any manner changed by reason of the announced doctrine. It was a limited announcement, restricted only to the application of the statute of limitations.

This is the precise situation in *Dunlop's Sons, Inc. v. Dunlop,* 18 N. Y. S. (2d) 818, also cited at page 39 of appellees' brief. The case is distinguished by the following statement of the court (Opinion p. 820):

> "The wrong pleaded is not a claim for profits in the sense in which that term is properly used in stockholders' actions."

The same distinction exists in the case of *Singer v. Carlysle,* 226 N. Y. S. (2d) 320, also cited at page 39 of appellant's brief and in *Wallace v. Lincoln's Savings Bank,* 89 Tenn. 630, cited at page 40.

Throughout appellees' brief there is no decision cited nor mentioned which directly or by inference decides that a shareholders "derivative suit" is not one for an accounting. Neither do appellees refer to any authority which, in such an action, requires a plaintiff to state in separate counts the items of wrongdoing.

Appellees in their effort to convince the court that appellant's complaint is founded upon several claims (Br. pp. 38-57) refer to the "salary agreement" item, and states (Br. p. 41),

> "the validity of agreements providing for incentive compensation is now too well settled to be successfully assailed as wholly void by any such applications as those mentioned"

and thereby evades the real fact presented by appellant's pleading to the effect that it was the profits obtained by the *fraudulent use* of the agreement for which appellant seeks an accounting. It is the only thing appellant can do to protect the "corporation" and this is true even though in an academic sense the corporation acting through an innocent board of directors *might* have maintained an action at law for money had and received. The form of action which the corporation might institute in no manner alters the necessity and the right of a shareholder to maintain his action in equity as one for an accounting. Appellees, in their argument with respect to the so-called second (2nd) item relating to "Walston & Co." and the alleged fifth (5th) item relating to the disbursement of money in "stirring" the market for Transamerica stock, make the same erroneous argument with respect to the nature of the transactions when considered in the light of relief being sought by a shareholder for the benefit of the corporation in a "derivative action." The equitable nature of such a suit and the fact that it is directed against trustees for an accounting for fraudulent and *ultra vires* acts cannot be changed into an action at law requiring its items separated into counts merely because the corporation could have sued at law upon some of the items involved.

Appellees fail to cite any authority in support of such a proposition.

Appellees in their attempt to show that appellant's second amended complaint should be separated into five separately stated claims also attempt to separate the participants by stating (Br. p. 46)

> "Passing over for later consideration the charges of conspiracy it will be observed that the participants in each transaction are not 'the same individuals.'"

The error in this observation is that in point of law, under the *admitted facts* set forth in appellant's pleading, the participants in each item of the transaction *are* the "same individuals".

At pages 43 and 44 of their brief, appellees refer to the case of *Bremner v. Leavitt,* 109 Cal. 130, which appellant discusses at pages 98, 99 and 100 of her opening brief, and quotes therefrom a portion of the decision which appellant overlooked, *and which omitted portion is the very essence of the principle for which we contend.* The omitted portion which appellant mentions is here repeated as follows:

> "Partners cannot sue one another at law for any breach of duties or obligations arising from that relation. This can only be done in chancery by asking a dissolution and accounting, and, if damages accrue from any cause in such proceeding, they must be adjusted by some appropriate method in that tribunal."

This statement makes it plain that if injury, called damages, accrued from any breach of duty or obligation arising from a partnership relation the same must be adjusted in chancery by seeking a dissolution and *accounting.* Part-

ners cannot sue one another at law for a breach of duty arising from the partnership relation. This is precisely the situation in the present action. The appellant shareholder cannot sue the delinquent directors to recover damages at law. Such injury can only be adjusted by the appropriate method of accounting in equity.

At page 45 of their brief appellees make some short comments with respect to *Veronia v. Sup. Coal & Ice Corp.,* 290 N. Y. S. 447; *Blake v. Boston Development Co.,* 50 Utah 347, and *Kilbourn v. Sunderland,* 130 U. S. 505, which together with *Bremner v. Leavitt, supra,* are discussed by appellant at pages 98 to 103 of her opening brief. Appellees' comments seem wholly insufficient to weaken those decisions as bearing upon and supporting appellant's claim with respect to an action for an accounting being a single action irrespective of the varied nature of the items or transactions involved. We see no reason to enlarge the argument contained in our opening brief upon the subject.

Again we are forced to draw attention to appellees' incorrect statement (Br. p. 47) to the effect that appellant is seeking to recover definite sums for each item mentioned in the pleading. Counsel for appellees have obviously failed to consider the "pleading" with respect to the nature and extent of the injury suffered by the corporation and have also failed to take cognizance of the nature of the injuries whereby a court can only strike a true balance through an accounting according to established practice. There is no other way to reach the complicated matters involved and arrive at a just and correct decree.

As an additional illustration of appellees' erroneous reasoning we refer to page 49 of their brief wherein it is stated:

> "But appellant has not charged 'delinquent trustees' with a 'general wrong'. No single substantive wrong is recognized under California law merely because the defendants are 'delinquent trustees'. This is made plain by the provisions of Section 427 of the California Code of Civil Procedure which provides that * * * If separate and distinct transactions became a 'general wrong' because perpetrated by 'delinquent trustees' there would be no reason for the foregoing provision of Section 427 of the Code of Civil Procedure."

Appellees' statement that as "delinquent trustees" they are not charged with a "general wrong" is so definitely incorrect that argument seems unnecessary. The "general wrong" is found by interpreting the appellants' "pleading" as a whole and not by the device of separating the same for the purpose of academic discussion. *The "general wrong" lies in the fact that appellees and their co-conspirators organized, operate and maintain the corporate structure for their sole individual use, gain and profit. The appellants' action on behalf of the "incompetent" corporation is one to compel its delinquent trustees to account for their secret profits and the corporate losses occasioned thereby.* There could be nothing more general in its scope than a case of this character. *It is directed against each and every individual who served as a director of the corporation and who contacted, aided, abetted and approved the general scheme so far successfully conducted.*

In this regard it must be remembered that appellant's action is not directed against strangers or third persons

dealing with the corporation whereby actions at law may have arisen and which for business reasons or matters of policy the directors deem it unwise to pursue. Appellants' action is directed against all the corporate directors and those who aided and abetted them in performing fraudulent and *ultra vires* corporate acts. We again assert that the substantive law of Delaware governs the law applicable in this case (*Erie Railroad Company v. Tompkins*, 304 U. S. 64) and therefore the directors and officers are express trustees for the stockholders and the corporation (*Cahall, Receiver, v. Lofland*, 12 Del. Chancery 290 at p. 305) and if not so considered by this court yet they became trustees of a constructive trust which was created by their own breach of fiduciary duties. (*Johnston v. McCluney*, 80 S. W. (2d) 898, 2d Syllabus Opinion, pp. 901-902.)

We are not aware that Section 427 of the California Code of Civil Procedure has any applicability whatsoever to the present action. We are here governed and controlled solely by Rule 10(b) of the Federal Rules of Procedure which in and of itself is not mandatory and should not be applied for the reasons cited in our opening brief. (Br. pp. 97-111.)

At pages 50 and 51 of appellees' brief comment is made with respect to the case of *Bowman v. Wohlke*, 166 Cal. 121, upon which appellees appear to greatly rely. Among other things, our reference thereto (App. Op. Br. p. 109) is criticized . We distinguished the case because it is a direct law action against certain individuals to recover damages for malicious prosecution, slander and trespass the redress of which has no place in equity nor in a suit for an accounting for the abuse of a trustee relationship.

Appellees, at pages 51 and 52 of their brief, in criticizing our point, stated:

> "But as we have already shown this remark is predicated upon the erroneous assumption that because appellant is before us in equity her position is different from that which would have been the case had Transamerica or its subsidiaries brought the action."

Concerning the foregoing remark, we respectfully but firmly urge that appellant is in a different position from the Transamerica Corporation and can only maintain a derivative suit in equity of the nature here presented.

We refer to the case of *United Copper Securities Co. v. Amalgamated Copper Co.* (2d Cir.), 223 Fed. 421 wherein it is said (Opinion pp. 422-423):

> "We think that a stockholder's right to assert a cause of action belonging to the corporation depends upon allegations that the corporation is acting fraudulently, in breach of trust, or *ultra vires*. For this reason he must go into equity. On the other hand, there appears to us to be no ground for holding that stockholders may bring actions at law in the name of the corporation to recover money damages or specific property whenever the corporation refuses to do so. Aimes v. American Telegraph & Telephone Co. (C. C.) 166 Fed. 820. Such a practice would be likely to create great confusion and tend to take unnecessarily away from the corporation the management of its own affairs."

The case of *Bachus-Brooks Co. v. Northern Pacific Railway Co.* (8th Cir.), 21 Fed. (2d) p. 4, is a minority stockholders' action in behalf of the corporation predicated upon the proposition that the Northern Pacific elects

and dominates a majority of the Board of Directors of the corporation for whose benefit the action was instituted and that in the transactions complained of such majority of the Board of Directors failed to faithfully serve the interests of the corporation but on the other hand managed and operated the corporation not for the benefit of its stockholders but for the benefit of the Northern Pacific Railway Co. *The action is one for an accounting and involves many items of wrongdoing.* There is no question of concealment or want of knowledge on the part of the complaining stockholder.

In determining that the statute of limitations of the State of Minnesota did not apply to that character of action (which will be hereinafter discussed under another part of this brief), because the case falls within the *exclusive* equitable jurisdiction of the court uses the following language (Opinion pp. 11-12):

> "The alleged *wrongs* complained of are *wrongs* against the Minnesota Company in which the complainant is a stockholder, and except through the corporation such *wrongs* had no relation to complainant. They did not directly injure complainant. Complainant was not affected by such *wrongs* except as every other stockholder was affected. There is no direct legal privity between the complainant, either individually or as a stockholder, and the respondents. As such stockholder, the complainant has an interest in the Minnesota Company and in the conduct of its officers affecting its property, *but this interest is equitable, and not legal, and it gives the complainant no standing in a court of law. Consequently the complainant cannot enforce a cause of action in behalf of the Minnesota Company in an action at law. His sole remedy is in equity.* . . .

> "The interest which the complainant seeks to enforce and protect is equitable. It is the existence of this interest which enables complainant to invoke the jurisdiction and aid of a court of equity. Complainants sole remedy for the protection of his equitable interest under the circumstances is in equity. Therefore, usually the case falls within the exclusive, rather than the concurrent jurisdiction of equity."

We again refer to the case of *Johnston v. McCluney*, 80 (S. W.) 898, wherein the controversy arises out of the sale or disposition by the defendant firm, but without the plaintiff's knowledge or consent, of certain securities owned by plaintiff, which had been purchased by her through the defendant firm but had not been delivered to her, with respect to which the plaintiff sought to have a trust declared in plaintiff's favor for the *amount of the proceeds of the sale with interest and that defendant be required to render a true account to plaintiff of such proceeds* and that judgment be entered against the defendant requiring payment to plaintiff of the total amount found to be due.

The defendant in that case, as in the present case, objects to the sufficiency of the pleading upon the ground that it did not allege facts sufficient to establish jurisdiction in equity for an accounting.

In holding that there was no merit in such objection the court makes the further statement which is precisely applicable to appellants pleading in the case at bar (Opinion p. 902):

> "The basis for equitable jurisdiction in a suit for an accounting is the inadequacy of the legal remedy, *and such jurisdiction has particular application in*

cases where a fiduciary or trust relation exists. . . . In other words there must be some distinct ground shown for invoking the jurisdiction of equity to which the demand for an accounting will be fairly incidental or ancillary. since a mere demand for an accounting, unless founded upon some recognized ground for equitable relief, will not serve to establish the inadequacy of plaintiff's resort to law for a remedy. . . .

"*In this instance the existence of a fiduciary relaitonship between plaintiff and the firm, and the creating of a trust in her favor, were sufficiently pleaded as we have already shown; and of course the enforcement of the trust thus created by operation of law was a matter of pure equitable cognizance.* But what was the amount of the trust for which defendant is sought to be charged? Plaintiff has pleaded her ignorance of the exact amount of the proceeds of the sale on account of which she asks the accounting of defendant as ancillary to and in aid of the trust which she asks to have adjudged as the basis of her cause of action. *It may well be that the account was not a complicated one, and indeed we now know that it was not; but inasmuch as plaintiffs case was otherwise one for equitable jurisdiction, she was fully warranted in asking the court to require defendant as trustee to account for the trust funds in his possession to the end that a judgment might be rendered in her favor for the balance found to be due after taking the account.*"

As heretofore stated, even though we treat the appellees as fiduciaries as distinguished from express trustees, for the purpose of appellant's action they are one and the same and require an action for an accounting to redress

the wrongs committed whether they be express trustees or trustees of a constructive trust arising from the wrongs. All this is true according to the decision cited irrespective of the involved or complicated nature of the account. In the present case however we can hardly conceive of an account between trustees and beneficaries being more highly involved or largely complicated.

At pages 49, 50, 51 and 52 of appellees' brief, the following additional cases are cited in support of the argument presented upon this subject, namely:

Kuhn v. Pacific Mutual Life Ins. Co., 37 Fed Supp. 100;

Connor v. Southern Ry. Co., 1 F. R. D. 410;

Chambers v. Nat. Battery Co., 34 Fed. Supp. 834;

American Foman Co. v. United Dye Wood Corp., 1 F. R. D. 171;

Ingenuities Corporation of America v. Tran, 1 F. R. D. 578;

Bicknell v. Lloyd-Smith, 25 Fed. Supp. 657;

Green v. Davies, 182 N. Y. 503;

More v. Finger, 128 Cal. 313.

We have carefully examined these decisions and submit each of the same to be wholly inapplicable to the point here under discussion.

The first above mentioned case of *Kuhn v. Pacific Mutual Life Insurance Co.*, 37 Fed. Supp. 100, is *not* a shareholders derivative suit instituted against directors of a corporation for fraudulent and *ultra vires* acts. It is merely an action at law between an individual and a corporation upon an insurance policy to recover several disability benefits which the District Court considered should be separately stated.

The case of *Chambers v. National Battery Co.,* 34 Fed. Supp. 834, is an action to recover damages for libel and slander wherein separate counts were required. This is a Missouri case wherein under the law a jury adjudicates the law in libel cases and the judge declares the law in slander cases. It has nothing whatever to do with the case here presented by appellant's pleadings.

The case of *Bicknell v. Lloyd-Smith,* 25 Fed. Sup. 657, cited by appellees is an *action at law* upon a written guarantee of the payment of corporate bonds. It also has nothing to do with the case such as here presented by appellant. It should take no argument to disclose the inapplicability of this case to the point sought to be made by appellees.

It is likewise true that in the case of *Green v. Davies,* 182 N. Y. 499, relied upon by appellees that the action is one *at law* wherein the court held that a cause of action for slander cannot be joined with one for malicious prosecution. We fail to see its applicability to the pleading here presented.

In the case of *Moore v. Finger,* 128 Cal. 313, cited by appellees the complaint was held to state a cause of action to recover the possession of a note owned by the plaintiff even though it contained a statement that the defendants had converted the note to their own use. We fail to find any similarity between this case and the one under consideration.

The case of *Conner v. Southern Railway Co.,* 1 F. R. D. 410, involves a complaint wherein two causes of action were commingled and set forth in one count of the complaint, one based upon statutory grounds and one based upon common law grounds. Defendant's motion to strike

the said count was granted by reason of Rule 10 (b) and the State Procedure. The decision does not disclose the precise nature of the action but it appears to be an action at law and apparently involves no trust relationship nor request for an accounting for *fraudulent* or *ultra vires* acts nor for the abuse of the fiduciary relationship. We are unable to perceive its applicability to the present action.

In *American Fomon Co. v. United Dye Wood*, 1 F. R. D. 171, the action involves a patent infringement and the recovery of damages for an unlawful appropriation of an invention. The District Judge granted a motion to dismiss by reason of an opinion given by another judge in the same matter at a prior date because, in the opinion of the former judge, he thought the bill "sets forth several causes of action" but did not intimate a view as to the sufficiency of any thereof. The court finally in deciding the case merely reaffirmed the former judge's opinion but granted leave to amend. The case does not seem to involve the equitable features presented in the action at bar.

In the case of *Ingenuities Corporation of America v.* Trau, 1 F. R. D. 578, it appears that the complaint as a whole was verbose and vague, the allegations of fraud, deceit and conspiracy were sprinkled indiscriminately throughout and some doubt existed with respect to the diversity of citizenship, creating the possibility that as to some of the claims the court lacked jurisdiction. The precise nature of the action is not disclosed in the decision except that it is one for unfair competition, unfair trade practices, fraud, deceit, conspiracy, infringement, violation of trademarks and violation of license contract and other rights of the plaintiffs. It is apparently an action

between parties dealing at arms' length for damages and possibly injunctive relief. It involves none of the attributes of the present case regarding accounting for trust violations.

At pages 53 to 57 of their brief, appellees discuss and attempt to apply Rule 10(b) to appellant's claim as set forth in her second amended complaint. At the outset of our reply to this argument we mentioned the uncontroverted fact that the record upon this appeal affirmatively discloses that the appellees' several motions for separate statements were not decided. The court made no ruling thereon. The motions stand abandoned. They have no purpose on this appeal except in so far as the subjects thereof might be considered upon the motions to dismiss.

In this connection we cite the following decisions:

In the case of *Winter v. Bostwich,* 212 Fed. 884 (7th Cir.), the complainants moved to amend their bill but the record did not show that any ruling was made on the motion nor that complainants asked for a ruling or assigned error on the ground that the court did not rule. It was held that complainants' right to amend could not be reviewed on appeal *as the question was not before the court for consideration.*

In *General Motors Co. v. Swan Carburetor Co.,* 44 Fed. (2d) 24, 2d Syl., Opinion, p. 25, it is stated:

> "Under the well settled practice which we are very often being called upon to apply, we cannot review a finding of fact to see whether it is based on any substantial evidence; *nor can we examine any question of law, unless the point was distinctly presented to the court below and ruled upon,* during the progress of the trial and proper exceptions were then taken." (Italics ours.)

In *Metropolitan Life Ins. Co. v. Armstrong,* 85 Fed. (2d) 187, 22 Syl. Opinion p. 193, the following language is used:

> "In any event there was no ruling on the objection, and hence no exception was saved. In the absence of either a ruling or an exception the alleged error can, of course, not be reviewed."

In *Gibson v. Luther* (8th Cir.), 196 Fed. 203, at page 204, the doctrine is thus stated:

> "As the trial progressed, objections of vital and controlling importance were interposed to the introduction of deeds and other documentary evidence but these objections were not passed upon by the court and no exceptions were saved by either party to any adverse ruling thereon. This precludes review of any of these rulings (objections) as we can act only on exceptions duly saved and assignments of error predicated thereon."

From the foregoing decisions and many others which could be cited, it is clear that appellant in this case could not predicate error upon any point *unless passed upon by the trial court.* We feel safe in saying that for the purpose of this appeal, at least, each and all of respondents' motions which remained undetermined by the trial court are thereby abandoned including their motion to require appellant to separately state claims. The subjects of each all of respondents' motions which were not passed upon by the trial court (Appellees' Br. p. 19, Subd. 2, 3 and 4) are not involved in this appeal and it is our thought that as we are precluded from a discussion thereof the respondents should likewise be estopped. This means that a discussion of the question concerning separate statements

of several claims by appellant should only be considered upon the merits with respect to appellees' motions to dismiss. This appellees do in their argument Number II (Br. pp. 37-57) in reply to Part IV of appellant's brief, pages 97 to 111.

Just why respondents attempt to claim that appellant violated an order of the trial court in filing her second amended complaint without a separate statement of several claims, in the face of the fact that the question was argued and determined upon its merits by the trial court and is now so argued and presented by appellees, does not appear.

Our position on this matter is that appellant's statement of claim or cause of action if divided and each item treated as an independent claim or cause of action would result in great confusion and directly violate Federal Rule of Procedure 10(b).

Replying to Appellees' Argument No. III.
(Brief pp. 58-92.)

Part "Two" of appellant's opening brief (pp. 69-87) is devoted to a discussion demonstrating the error of the trial court in granting appellees' motions to dismiss on the ground that the action was filed too late. Whether or not the trial court applied the California statute of limitations or the doctrine of "laches" we do not know but we do know that appellees' answering argument to that part of our opening brief is far from a sufficient reply.

Instead of showing the inapplicability or insufficiency of appellant's opening brief, appellees' argument fails

to recognize the admitted concealment of their own wrongs, as alleged in the appellant's pleading, and also fails to discuss the doctrine of "laches" from the viewpoint presented in appellant's brief.

Appellees' entire discussion of this subject consists of and is based upon the incorrect assumption that the point is determined by the California statute of limitations and the California decisions with respect thereto. A plain and frank discussion of the doctrine of "laches" when applied to a concealed fraud involved in a suit only cognizable in equity is completely avoided. We realize and do not hesitate to assert that the courts in some cases refer to a State statute of limitations and the doctrine of "laches" in terms which might convey the thought that they are one and the same. This is not the case. They are in some respects similar but they are not identical.

Statutes of limitations are purely matters of legislative creation, in the absence of which, lapse of time does not of itself constitute a defense to the right to enforce a liability. They are statutes of repose and are enacted upon the theory that one having a well founded claim will not delay for an unreasonable time to enforce it. However, they are arbitrary with respect to the time limited, which is definitely measured by the statute and from which there can be no deviation no matter how justified the same may be from a factual standpoint. On the other hand the doctrine of "laches" is an equitable principle founded in the factual circumstances of each case and based, not upon an arbitrary time limit, but upon the fact that in each case equity requires diligence on the part of a plaintiff in order that a defendant may not be prejudiced by undue delay as demonstrated by the decisions cited in part

two of our opening brief (pp. 69 to 87, incl.). This is undoubtedly the reason that Rule 8(c) requires the defense of "laches" to be pleaded in an answer. The rule is especially applicable in a case of concealed fraud which may be only accidentally discovered.

Appellees' argument fails to take the elements of "laches" into account and thereby evades a direct answer to appellant's argument upon the subject.

As we understand the doctrine it is based wholly upon the very early principle that equity demands diligence and lack of diligence constitutes "laches" which is applicable where the adverse party has been misled or otherwise substantially prejudiced. It is our thought, which we firmly urge, that the California statute of limitations is not applicable and that the concealment of the fraud and the circumstances of its discovery by appellant disclosed diligence on their part as distinguished from a lack thereof. Counsel for appellees in their argument with respect to the statute of limitations again seek to divide and destroy plaintiff's pleading by detailed analysis which views the pleading in a light which is unwarranted *when construed as a whole.*

Appellees in their effort to create some confusion with respect to appellant's position upon the subject here discussed incorrectly states (Brief p. 58):

> "Appellant contends that since, under rule 8(c), it is provided that laches and the statute of limitations must be affirmatively set forth as a defense a motion to dismiss under rule 12(b) is not proper, and cites Dirk Ter Haar v. Seaboard Oil Company, 1 F. R. D. 598."

A statement to this effect does not appear in appellant's opening brief. Our statement regarding the necessity for a trial upon the merits of the defense of laches in the present action upon a formal issue thereof and a full and complete development by evidence of all the facts and circumstances of the case is followed by the following statement which under the circumstances we deem necessary and proper to repeat (Br. p. 84):

> "The elements of laches or the absence thereof call for such an investigation. Except in very rare cases where neglect or lack of diligence is *clearly apparent* upon the face of a complaint, such issue is factual. In the present action, appellant desires the appellees to face a trial upon the merits of the controversy that, among others, the issue of 'laches' if properly and sufficiently presented, may be fairly tried and appellant's case not erased by academic interpretation upon 'motions to dismiss'."

We did cite the decision rendered by Judge Beaumont in *Dirk Ter Haar v. Seaboard Oil Company,* 1 F. R. D. 598, wherein the following decisions are cited in support of the court's ruling and which, contrary to appellees' judgment in the matter may constitute the weight of authority, namely:

Patsavouras v. Garfield, D. C. (New Jersey), 34 Fed. Sup. 406;

Munzer v. Swedish American Line, D. C. (New York), 30 Fed. Sup. 789;

Holmberg v. Hanaford, D. C. (Ohio), 28 Fed. Sup. 216;

Raker v. United States, D. C. (New York), 1 F. R. D. 432;

Baker v. Sisk, D. C. (Oklahoma), 1 F. R. D. 232;

Nordman v. Johnson City, D. C. (Illinois), 1 F. R. D. 51;

United States v. Earling, 39 Fed. Sup. 864, 5 Fed. Rule Service 105;

United States v. Arthur, 23 Fed. Sup. 537;

Reconstruction Finance Corp. v. Central Republic Trust Co., 11 Fed. Sup. 976.

With respect to the authorities cited by the appellees at page 59 of their brief to which they refer as constituting the weight of authority the following observations may be in order.

The case of *Abraham v. San Joaquin Cotton Oil Co.* (D. C. S. D. Cal.), 46 Fed. Sup. 969, is an *action at law* to recover wages and liquidated damages under the Fair Labor Standards Act and is directly subject to the State statute of limitations by the "Conformity Act."

In the case of *A. G. Reeves, Steel Const. Co. v. Weiss,* 119 Fed. (2d) 472, it appears that the action is *one at law,* created by statute, to recover taxes claimed to have been overpaid. The case does not involve a motion to dismiss by reason of the statute of limitations. The plaintiff's case was dismissed by final judgment after a trial wherein the statute of limitations was not invoked by a motion or a pleading but was invoked by the court because the question of the time limit was a part of the plaintiff's action and not only barred the *remedy* but also *destroyed the liability* of the appellees to refund the taxes.

Wright v. Bankers Service Corp., 39 Fed. Sup. 980, is also a common law action to recover damages for

fraud under the "Securities Act" of 1933 and amendments thereto designated in the United States Code as Sections 77k and 77o, wherein the "time limit" destroyed the liability sought to be enforced. To institute an action within the time especially limited by the act is a condition upon which the right of action depends and must be alleged and proved.

The case of *Cramer v. Aluminum Cooking Utensil*, 1 F. R. D. 741, is an *action at law* to recover damages for the death of a person and has nothing to do with an equitable proceeding involving the rule of diligence or the doctrine of laches. In this case the defendant affirmatively interposed the statute of limitations as a defense and sought to require a reply thereto by the plaintiff. The court merely held that the defendant's motion for an order requiring the plaintiff to reply be denied. We see no similarity with nor applicability to the case at bar in this decision.

In the case of *Barnhcart v. Western Maryland Ry. Co.*, 5 Fed. Rule Service, 103, the action was treated as a *common law suit* for wages and damages for a wrongful discharge and the complaint disclosed upon it's face that the cause of action arose more than 19 years prior to the institution of the action and nothing was alleged to excuse the long delay. Even in this case the District Court held that ordinarily the defense of limitations must be interposed by an answer except where the bar of limitations *conclusively appears from the complaint.*

The decision in *Pierson v. O'Connor*, 5 Fed. Rule Service, 104, contains no statement with respect to the nature of the action nor the contents of the complaint and is of little value upon the question involved.

A careful comparison of the decisions to which we refer with the cases cited by appellees, concerning the non-availability or the availability of the statute of limitations upon a motion to dismiss, discloses a weight of authority in favor of appellant's contention and, even without respect to the weight of the decisions, it becomes clear, upon a reading of the cases, that our original statement to the effect that "except in very *rare cases* where neglect or lack of diligence is *clearly* apparent upon the face of a complaint, such issue (laches) is factual" is correct. In the present action it can never be precisely and justly determined until the grossness of the appellees' fraud, the extent and nature of their concealment, all the circumstances with respect to the lack of knowledge, the unavailability of means of knowledge and all the circumstances of her discovery of "suspicious circumstances" leading to the actual discovery of the facts set forth in her pleading are considered from the evidence as a whole under a proper and formal issue upon which findings of fact and conclusions of law may be made and entered by the trial court.

At this point it seems appropriate to again refer to the case of *Bachus-Brooks Co. v. Northern Pac. Ry. Co.*, 21 Fed. (2d) 4. As heretofore stated this is a stockholder's suit prosecuted by a minority stockholder in behalf of the corporation, predicated upon the proposition that the Northern Pac. Ry. Co. elects and dominates a *majority* of the Board of Directors of the defendant corporation in which the plaintiff is a stockholder, called the Minnesota Company and that in the transactions of which complaint is made such *majority* of the Board of Directors failed to faithfully serve the interests of the Minnesota

Company and its stockholders, but, on the other hand managed and operated such company for the benefit of the Northern Pac. Ry. Co. This is the identical situation in the case at bar which definitely appears, from the admitted allegations of the appellant's "pleading," except instead of operating the plaintiff's corporation for the benefit of some other corporation, the appellees' general wrong consists *in directly maintaining and operating it for their own individual and private gain.*

In the case here discussed it was expressly contended that the statute of limitations of the State of Minnesota constituted a bar to plaintiff's recovery, asserting that the suit was within the concurrent and not the exclusive equity jurisdiction and that in such cases the Federal courts are bound by the State statutes of limitation which govern actions at law.

The court, after holding that a derivative shareholder's action is within the exclusive jurisdiction of equity, determines that the state statute of limitations is not applicable to such a case in the following language (Op. p. 12):

> "No doubt the right of a stockholder to maintain a suit in equity in behalf of the corporation after the running of the statute of limitations should be limited to extraordinary cases *where there are unusually strong equities in favor of the complainant. We think it not difficult, however, to conceive of such a case.* Suppose the same persons constituted the officers and directors of two corporations, that they were unfaithful to their trust in respect to one of the corporations and carried out a transaction to the detriment of such corporation, and for the benefit of the other corporation, *and that they concealed such trans-*

action from the stockholders of the injured corporation until after the running of the statute of limitations; could it be said that a stockholder of such injured corporation on discovery of the facts could not obtain relief from such a transaction in a court of equity? *We think not.* For these reasons, we believe that the principles of the 'doctrine of laches,' and *not the provisions of the statute of limitations,* should condition the time within which a stockholder must commence such a suit in behalf of the corporation.

"Is the complaint barred by the doctrine of laches from complaining of wrongs which occurred more than six years prior to the filing of the bill?

"The general principles which control the application of the 'doctrine of laches' were stated by Judge Sanborn in Kelley v. Boettcher (C. C. A. 8) 85 F. 55, 62, as follows:

" 'In the application of the doctrine of laches, the settled rule is that courts of equity are not bound but that they usually act or refuse to act in analogy to, the statute of limitations relating to actions at law of like character. (Citing cases.) The meaning of this rule is that, under ordinary circumstances, a suit in equity will not be stayed for laches before, and will be stayed after the time fixed by the analogous statute of limitations at law; *but if unusual conditons or extraordinary circumstances make it inequitable to allow the prosecution of a suit after a briefer, or to forbid its maintainance after a longer, period than that fixed by the statute,* BUT WILL DETERMINE THE EXTRAORDINARY CASE IN ACCORDANCE WITH THE EQUITIES WHICH CONDTION IT. * * *"

This indeed is a refreshing decision and constitutes a complete answer to the entire argument presented by the

appellees in Part III of their Brief (pp. 58 to 92, incl.). The case definitely and unequivocally determines that in a case of this nature the California statute of limitations *is not applicable and that there can be no determination of the question of "laches" upon the motions to dismiss because the equities have to be balanced upon a trial of the issue in order to determine whether or not it is inequitable to allow the prosecution of the action after a briefer, or to forbid its maintenance after a longer, period than fixed by the statute.*

In the reported case here discussed it definitely appears that the defense of "laches" *was tried upon its merits* and was sustained because the evidence disclosed without contradiction that the plaintiff stockholder had complete knowledge of all the matters complained of *since their inception* which was more than twelve years prior to the institution of the suit. In the present action, considered from the face of the pleading, there is not the slightest showing that the plaintiff had any knowledge nor the means of knowledge with respect to the misuse of the corporate structure and its funds and property until the 27th day of April, 1939, *when means of knowledge were accidentally discovered* from the *quasi* judicial proceedings before the Securities Exchange Commission in *Washington, D. C.,* which discovery was followed by investigations which led to the filing of this action on April 16, 1941, only two years and eleven days after "means of knowledge" was uncovered. Appellees cannot and have not presented any argument which can alter this situation. The appellants pleading affirmatively shows that all of the wrongful acts of the appellees were buried, completely and successfully concealed and all means of knowledge

likewise fully covered. These are admitted facts which, even upon a motion to dismiss, cannot be avoided in considering the question of laches.

At pages 62 to 69, inclusive, appellees again attempt to apply the California three year statute of limitations by arbitrarily dividing plaintiff's claim into five separate transactions. We see no point in using space in reply to this character of argument. Our opening brief and the previous remarks in this brief disclose that appelalnt's claim is founded upon *a single claim or cause of action* and is not to be separated into items for the purpose of attempting to apply the statute of limitations which may be invoked only in common law actions.

At pages 69 to 85, inclusive, of their brief, appellees present the argument that appellant's pleading does not allege sufficient facts to excuse the failure to commence the same within the statutory period of three years. This, of course, assumes a false premise and an argument limited solely to the statute of limitations as distinguished from the "doctrine of laches." The argument made and the cases cited when viewed in the true light of appellant's "pleading" are all irrelevant. They have no bearing upon the conditions and circumstances with respect to the relationship of the parties, the nature of the action, the concealment of the wrongs and the manner of discovery, all of which make it inequitable to deny relief upon the ground of "laches." We make this statement from the face of the pleading in view of the fact that nowhere in appellees' brief have they made answer to the legal effect of "concealment" in cases of this character. Appellees dwell upon the theory of "legal discovery" as based upon the interpretation of the California Statute of Lim-

itations given by its courts *but they do not refer to concealment which from early English law has always kept cases alive which deal with fraud.*

Counsel for appellees in their attempt to apply the California three year statute of limitations to the item which they denominate "the salary agreement transaction" again by argument attempt to divide the same into the separate payments made thereunder and treat the same as mere evidence of damage arising from a single fraudulent act, which, for the purpose of an action at law could have been prospectively estimated. Appellees state (Br. p. 64)

> "in this case the statute of limitations began to run either at the time of the perpetration of the alleged fraud or at the time of the discovery".

In support of this statement the following cases are cited:

Thayer v. Kansas Loan Co., 100 Fed. 901;

Agee v. Virden Packing Co., 15 Cal. App. (2d) 691;

Greenberg v. Du Bain Realty Corp., 27 Cal. App. (2d) 111;

Sanders v. Sanders, 117 Cal. App. 231;

Bradbury v. Higgenson, 167 Cal. 553.

While we sincerely believe and firmly assert that a discussion of the California statute of limitations is irrelevant yet as appellant's claim is clearly not barred by such statute, but was instituted less than three years from actual or legal discovery of the fraud we deem it proper to reply to appellees discussion.

The case of *Thayer v. Kansas Loan Co.*, 100 Fed. 901, cited by appellees at pages 64 and 65 of their brief is an

action at law to recover money alleged to have been obtained from the plaintiff by the fraud and deceit of the defendants. Under the "Conformity Act" the question of "time" in which to institute the action was governed by the Kansas statute of limitations which with respect to actions for relief on the ground of fraud provides "the cause of action in such case shall not be deemed to have accrued until discovery of the fraud". The act is similar to the California statute with the exception of the period of time.

In that case it was claimed by the plaintiff that the statute of limitations did not begin to run until after certain foreclosure proceedings had been concluded and a sale of the premises made and the damages determined. The court, under the applicable Kansas statute correctly held that the cause of action accrued upon *discovery* of the fraud which with diligence the plaintiff could have discovered within the two year period.

The court in its opinion makes it clear that the decision is not applicable to the case at bar wherein, in addition to the matter mentioned by appellees, the court states as follows (Op. p. 903):

> "Under this statute the cause of action is not deemed to have accrued until the discovery of the fraud, but it is not sufficient to allege or to show merely that the defendant had no notice of the fraud, in order to defeat the plea of the statute of limitations. *It must be also alleged and proved that there has been such concealment as would prevent a person exercising due diligence from discovering the facts.* * * * The transaction between the plaintiff and the defendants took place in 1886. There is nothing

shown in the petition why the plaintiff could not have discovered the true value of the mortgaged property, and the financial condition of the mortgagors, within two years thereafter, and certainly such discovery could have been made more than two years before the institution of this suit. There is no allegation or proof to show that he made any effort to ascertain these facts. Plaintiff merely relied upon the statements made to him by the agents of the defendant trust corporation."

It will be observed that in the foregoing case there was no concealment of the alleged fraud and the means of knowledge were open to the plaintiff at all times. It was merely a case of lack of diligence which equity requires as a touch-stone for its jurisdiction.

We are at a loss to understand wherein this decision is of any aid to the appellees. We make no contention, even assuming the applicability of the California statute of limitations, that any cause of action ever accrued on behalf of appellant until the means of knowledge was accidentally uncovered and came to her attention on the 27th day of April, 1939.

The case of *Agee v. Virden Packing Co.*, 15 Cal. App. (2d)691, 694, cited at page 65 of appellees' brief is an action to recover money for fraud which was paid during a period of time ranging from nine to thirteen years prior to seeking relief. *The case involves no concealment and means of knowledge was open to the plaintiffs.* The complaint did not comply with the State rule of decision with respect to showing the circumstances under which the facts constituting the fraud were brought to their knowledge. We have no quarrel with this decision but fail to

see its applicability to a case of concealed fraud which could not be discovered with reasonable diligence as in the case at bar.

The case of *Sanders v. Sanders*, 117 Cal. App. 231, 234, cited by appellees at page 66 of their brief is an action to recover money due under a property settlement agreement but paid under a mistake when it was not due. *The* EVIDENCE *showed that the party in interest who was the defendant in the action discovered the mistake five years prior to the commencement of the action.* We are wholly unable to understand the applicability of this decision to the present action. We again state that it is our theory of the case that if the California statute of limitations does govern the case at bar instead of the "doctrine of laches" then appellant's action did not accrue until the "discovery" of the fraud which was within the statutory three year period and constitutes diligence. *Upon this subject it must be remembered that appellees' argument, based upon the interpretation of the California statute of limitations in question by it's courts, to the effect that "means of knowledge" constitutes a legal discovery of fraud as distinguished from an actual discovery is not the legal test in determining the question of "laches" as, in such case, there are many other elements to be factually determined in balancing equities as pointed out in our opening brief and herein restated.*

Referring to the case of *Bradbury v. Higgenson,* 167 Cal. 553, cited by appellees at page 66 of their brief, it will be noted that under the California State practice the statute of limitations applies alike to both actions at law and suits in equity and to that extent is distinguished from the Federal practice. This case is an action brought by a

lessor to recover rent due under a lease which the lessee had abandoned on account of an omission therein of a covenant to furnish water. *The means of knowledge were at all times open to the defendant, the mistake was not concealed, the defendant did not seek to present any equity such as exists in cases of fraudulent concealment.* Just what the decision has to do with a shareholders' "derivative suit" for an accounting with respect to secret profits, gains and corporate losses sustained through the operation of the corporation by delinquent directors and which are likewise concealed, we do not know. It is not pointed out in appellees' brief.

At page 69 of appellees' brief the point is made that according to the case of *Wood v. Carpenter,* 101 U. S. 134, 140, 141, a plaintiff must allege with particularity when the fraud was discovered, what it was, how it was made and why it was not made sooner. We submit that appellant's pleading definitely and certainly answers all these requirements. The discovery of "circumstances" leading to the subsequent discovery of the actual fraud is alleged to have occurred on April 27, 1939. The nature of the discovery is alleged to have been a part of certain *quasi* judicial proceedings before the United States Securities Exchange Commission pending in Washington, D. C. and the reason it was not made sooner is found in the admitted allegations of "concealment."

We also direct attention to the fact that the case of *Wood v. Carpenter* relied upon by appellees is *one at law* to recover upon promissory notes and bills of exchange. The Indiana Statute of Limitations with respect to relief against frauds was directly applicable and the strict rule of pleading, to escape the effect of the statute, is confined

to law actions. Even so, the plaintiff's reply to the plea of the Indiana statute was only held insufficient because the manner of concealment was not set forth but was merely alleged as a *general conclusion* to the effect that certain facts were concealed by means of fraud, perjury and certain devices with respect to which the plaintiff had no knowledge of facts so concealed. Bearing in mind that the statute of limitations of Indiana was there directly applicable and the conclusions of the pleader held insufficient, give no weight to the decision as applicable to the complete allegations of fact contained in the appellant's pleading regarding the manner, nature and extent of appellees' concealment. The guilty party will not advertise his own fraud. The frauds consist of matters which must be reflected by book of accounts, figures and designation of dealings. It is admittedly alleged that such records were by specific methods buried and covered beyond discovery by any person not acquainted therewith. The California cases cited by appellees at pages 70, 71, 77, and 78 of their brief add nothing to the potency of their argument upon the point in question.

At pages 78 and 79 of appellees' brief the point is made that to avoid the bar of the statute of limitations (assuming it to be applicable) it became necessary to show by appellant's pleading that the corporation involved was under a disability which prevented the statute from running and that the allegations of the pleading are insufficient for that purpose. In support of the argument there presented the following authorities are cited:

Whitten v. Dabney, 171 Cal. 621-629;
Baillie v. Columbia Gold Mining Co., 86 Ore.;
Starke v. Boggs, 289 Ill. App. 461.;
Texas Company of Mexico v. Ross, 43 Fed. (2) 1, 16.

In the first above mentioned case of *Whitten v. Dabney* the plaintiffs "as stockholders of the Dabney Oil Company sued defendants Dabney, Miley, and Butler, alleged certain factual impositions practiced by them upon the Dabney Oil Company resulting in great loss to that company. They asked for an *accounting* in behalf of the company against these defendants and a recovery into the treasury of the company of the amount which it might be determined that the company had been defrauded. *A conspiracy to commit these fraudulent acts was charged against the three men.* Their *control* of the corporation through its board of directors and the refusal of the corporation upon demand to prosecute the action is also set forth. Frederick E. Mason, another stockholder, petitioned for leave to intervene and permission was granted. His complaint in intervention set up the same wrongs pleaded by plaintiffs and joined with them in their prayer for relief.

A general demurrer was interposed to these complaints and sustained. So, also, was a demurrer raising the bar of the statute of limitations. From the judgment which followed, plaintiffs appeal in San Francisco, No. 6486. From that same judgment the intervener appeals in San Francisco, No. 6591. Both of these appeals present the same asserted error of the court in sustaining the general demurrer for absence of facts. Both, too, present a like question upon the bar of the statute of limitations."

From a reading of this decision it appears, as in the case at bar, that the complaint charges conspiracy, seeks an accounting from the defendants who in pursuance of a conspiracy between themselves and by means of a *control* of the corporation by a dummy directorate caused false dividends to be declared and paid out of the proceeds of the sale of the corporate stock, false credits to be entered

on the company's books whereby defendants individual indebtedness to the corporation were made to appear as having been paid and cancelled and for commissions upon the sale of treasury stock without authority from the corporation.

The various wrongs and injuries and the several items are included in one cause of action.

The court's summary of the complaint is found at pages 625, 626 and 627 of the opinion, and appears to be substantially similar to the pleading now before the court.

After summarizing the complaint the court in reversing the judgment of the trial court states. [Opinion pp. 627-29-30; App. p. 1.]

We are unable to perceive wherein appellees obtain any satisfaction or comfort from this decision. It expressly holds that the disability of the corporation occurs when its' *control* is in the hands of a board of directors accused of participation in the frauds. It does not hold that by reason of one minority so called innocent director the corporation becomes competent and is relieved from disability. The decision is in accord and supports the reply to appellees' argument No. II, to the effect that the pleading here involved states but one claim or cause of action.

Permit us to suggest that the complaint in the reported case was subject to the strict state rules of pleading with respect to "ultimate facts" while the pleading in the case at bar is governed by the Federal rules of procedure requiring only a short and plain statement of the claim to be construed as to do substantial justice.

In view of these material distinctions in the rule of pleading and by comparison of the pleading in the present action with the complaint in the reported case it becomes

clear that the pleading here discussed should be held sufficient.

The case of *Baille v. Colombia Gold Mining* Co., 86 Ore. 1, cited by appellees at page 79 of their brief is clearly not in point. In that case the suit was not brought in the right of the corporation but assuming that it stated such a cause yet there was no demand upon the board of directors of the corporation nor are they charged as being the guilty party. The plaintiff attempted to excuse his failure to make a demand upon the board of directors to institute the action by merely alleging that a certain stockholder had it in its power to control the election of officers and the conduct of the business of the corporation and that such stockholder was unwilling to and will not act in the matter.

This is not the case at bar and is in no manner comparable with the pleading in the present action.

On the other hand this decision directly supports the appellant in the present case with respect to her pleading stating but one count or cause of action.

The bill of the minority stockholder in the reported case which alleged a series of frauds committed by the defendants through the control of the corporation was held to state but one cause of action and in this respect the court cited the case of *Baillie v. Backus*, 230 Fed. 711, 716 and in determining that question said. [Opinion p. 15; App. p. 3.]

Referring again to our reply herein to appellees argument No. II, permit us to here show that the decision cited by the Oregon court, namely *Baillie v. Backus,* also is in accord and supports our contention discussed in that part of our argument to the effect that the various items of wrongdoing are not separate claims nor causes of action

but are merely items forming elements for a general accounting. In the *Baillie* case the court had a similar complaint under consideration with respect to which the following statement is made: [Opinion p. 716.]

> "Now, the bill of complaint in the present case does not seek a separate accounting, but an accounting by all the parties alleged to have been engaged causing the misappropriation, and, as appears from the theory of the bill, the cause is one against all the parties involved in misappropriating the funds of the Mining Company. Such is the case brought by the plaintiff, and by it he is entitled to have the suit proceed in the forum of his choice. Separate causes of action are not joined, but only a particularization of different items of misappropriation, all entering into and forming elements of the general accounting demanded."

We have carefully examined the case of *Texas Co. of Mexico v. Ross,* 43 Fed. (2d) 1, 15 and find nothing therein which in any manner relates to the sufficiency of appellant's pleading in the respect adversely criticized by appellees at page 79 of their brief. The decision merely points out that a parent corporation which controls a subsidiary corporation is not liable for a wrong or injury committed by the subsidiary corporation unless it had something actively to do therewith. This seems to be good law but it's applicability to the present case is entirely lacking.

At page 81 of Appellee's Brief it is claimed that if one director of a corporation, who is not under the dominion or control of the other delinquent directors, obtains knowledge of the transaction complained of the statute of limitations begins to run against the corpora-

tion. In support of this contention appellees cite the following cases:

Curtis v. Connly (1921), 257 U. S. 260, 66 L. Ed. 222;

Farmer v. Standeven (1938), 93 F. (2d) 959;

Hughes v. Reed (1931), 46 F. (2d) 435;

Grussemeyer v. Harper (1936), 187 Wash, 508, 60 P. (2d) 702;

Van Schaick v. Aron (1938), 10 N. Y. S. (2d) 550, 562.

The case of *Curtis v. Connly,* 257 U. S. 260, is not a shareholders derivative suit. It is a common law action by a receiver of a National Bank to recover, from former directors, losses sustained by reason of dividends paid out of capital and improper loans and investments made by the defendants. The statute of limitations of the State of Rhode Island was directly applicable to the action.

It is important to note that in this case there was *no fraudulent or other concealment* of the acts of the defendants and because three new directors were elected within the period of the statute of limitations *who were not in conspiracy with the defendants* notice of the wrongful acts was imputed to the corporation as such acts appeared from entries upon the corporate books and records and were not concealed.

The reported case is obviously inapplicable to the case at bar where each and all of the directors during the entire period of time are charged with the wrongs and their acts are alleged to have been concealed by certain and definite averments.

The case of *Farmer v. Standeven,* 93 F. (2d) 959, cited by appellees at page 81 of their Brief is also a case where the wrongful acts of the directors were not concealed and there were directors who were not charged with conspiring with the wrongdoers by reason of which notice of the wrongful acts was imputed to the corporation within the statutory period. The holding of the court that Opinion, pages 961-962, makes this distinction as follows:

> *"There was neither allegation nor proof of any conspiracy between Standeven and the other directors. There was neither pleading nor proof of active concealment on the part of Standeven.* On the contrary, the entire transaction was fairly and fully reflected on the books of the company. The other officers and directors were chargeable with notice of what the books of the company reflected and what reasonably prudent inquiry would have disclosed. The transactions were unusual and the books and records of the company reflected sufficient to put the other officers and directors on inquiry. They could have readily ascertained the market value of the stock on December 31, 1930."

The case of *Hughes v. Reed,* 46 F. (2d) 435, is also an action by a receiver of a National Bank against former directors to recover losses through loans made to officers of the bank which impaired its capital and surplus. After a general discussion with respect to the statute of limitations and the doctrine of laches the court, in holding that the character of the action permitted the application of the Oklahoma three years statute of limitations, determined that the action was bared because it commenced to run when the bank actually parted with the money loaned.

The court obviously based its decision upon *Cooper v. Hill,* 94 Fed. 582 and *Curtis v. Connly,* 257 U. S. 260 [see Opinion, p. 441] wherein in each case, as distinguished from the case at bar, the books of the corporation disclosed the transactions and there were no affirmative acts of concealment nor any charge of a conspiracy between new or any directors, having knowledge of the wrongs, with the defendants nor was there a charge of a conspiracy of silence.

The case of *Gurssemeyer v. Harper,* 187 Wash. 508, cited by appellees upon the point here discussed, does not appear to involve the proposition urged. It is a case where after the trial it was determined by the court that the plaintiffs had no cause of action against any of the defendants except for negligence of one or two thereof which presented an action at law only and was bared by the Washington two year statute of limitations. The charge of conspiracy was not sustained.

If this case is of any value to a decision in the present action it shows that in involved cases of the character of appellant's action, even the question of the statute of limitations should be tried upon its merits and determined from the evidence disclosing the entire transaction.

The case of *Van Schaick v. Aron,* 10 N. Y. S. (2d) 550, 561, 562, cited by appellees, appears more likely to support the sufficiency of appellant's pleading rather than the point urged by appellees. [Opinion pp. 561, 562; App. p. 3.]

It is indeed a desperate argument for appellees to urge, as an abstract proposition of law, that the knowledge of a so-called innocent director regarding the wrongdoing of other directors who control the corporation is *ipso facto*

imputed to the corporation for the purpose of applying the doctrine of laches or the statute of limitations. By failing to take action on behalf of the corporation with the knowledge so possessed such director is guilty of non-performance of an official obligation amounting to a gross disregard of duty and a breach of trust which in turn constitutes an act beyond the scope of his duty to the corporation and which is not imputed to it.

This principle is stated in *Dodge v. Woolsey,* 59 U. S. 331, 345. [App. p. 6.]

In the present action the pleading charges all the appellees, at all times, with the continued perpetration of all the wrongful acts and it is merely because of a hypothetical and alternative plea, now definitely authorized by the rules, that appellees present this point in the face of the admitted allegations of the pleading.

The mere *possibility* of some director ascertaining the acts of wrongdoing by other directors and failing to seek relief, being hypothetical and permitted as a matter of pleading, bears no relationship to laches or the statute of limitations.

Again referring to the case of *Van Schaick v. Aron,* 10 N. Y. S. (2d) 550, 561, 562, the court at page 561 refers to the following cases:

Smith v. Lyle, 59 S. D. 534;
Adams v. Clark, 22 Fed. (2d) 957;
Reid v. Robinson, 64 Cal. App. 46.

In the first mentioned case of *Smith v. Lyle,* 59 S. D. 534, the defense of the statute of limitations was tried upon the merits and not upon the face of the pleading. This case involves a claim that the statute ran against the

bank's creditors by reason of certain knowledge, of the wrongful acts in question, discovered by the Superintendent of Banks, prior to his taking possession of the bank's assets. It does not seem to apply to any point in the case at bar.

The case of *Adams v. Clark,* 22 Fed. (2d) 957, is a suit by a receiver against directors of a national bank for making illegal loans. It is not based upon the common law negligence of the defendants but upon a *statutory limitation* placed upon the extent of loans which, if violated, made the directors personally liable to the bank or to the stockholders or any other person who suffered as a consequence. The case is similar to the case at bar in that the corporation was at all times under the *exclusive control of the defendants.* The decision does not involve any proposition relating to knowledge of an innocent director being imputed to the banking corporation.

The case of *Reid v. Robinson,* 64 Cal. App. 46, mentioned in the reported case, is worthy of consideration. It involves a case where one of the stockholder plaintiffs was also a director of the corporation during the time that the frauds were perpetraated by the defendants, his co-directors. The case not only supports the appellant's pleading but shows that a trial is essential upon the defense of laches and the defense of the statute of limitations in order that a just decision may be reached and that the question of knowledge or means of knowledge of a director is factual. [Opinion pp. 55, 56; App. p. 4.]

The case here considered also supports appellant's contention that a shareholder's derivative suit to recover secret profits made through fraud of the directors is properly one of *accounting,* that there is no duty incumbent

upon the plaintiff shareholders to examine the books or the minutes of the corporation for the purpose of detecting fraudulent acts and that a defendant who is in any manner concerned in the wrong irrespective of the degree in which he participates and without reference to any benefit which he may receive therefrom is liable therefor. [Opinion p. 48; App. p. 4.]

Replying to Appellees' Argument No. IV.

(Brief pp. 93 to 112.)

This part of appellees' brief is an attempt to develop by mere argument and unwarranted assumption that the real relationship between the Transamerica Corporation and its subsidiary departments and instrumentalities is something different from that alleged in appellant's pleading. In this argument appellees also make some comment concerning the authorities cited in our opening brief upon this subject, but nowhere is the principle for which we contend weakened in its application to the pleading here involved.

After a careful consideration of appellee's argument in the respect noted, and the decisions cited, we feel safe in saying that appellees intend thereby to admit the doctrine of the "disregard of the separate entity" of a controlled corporation where recognition thereof results in an injustice but base their point upon the claim that (Brief p. 107):

> "No reasons of justice or equity have been advanced by appellant herein as to why the court should pierce the corporate veil of Transamerica's subsidiaries."

A complete answer to this line of reasoning is that these so-called subsidiaries are not, as yet, found to be independent corporate structures but on the other hand are alleged to be mere departments and instrumentalities of the Transamerica Corporation. The injustice of recognizing these departments as separate entities appears from the face of the entire transaction set forth in the pleading. The alleged corporate veil of Transamerica's subsidiaries is already pierced by the pleading, and appellant will be called upon to establish the allegations thereof.

We have read the case of *Greenburg v. Gianinni,* 140 Fed. (2d) 550, which appellees cite (Brief pp. 107, 108), and find no fault therewith. It does not relate to a double derivative suit but on the other hand it does show that a shareholder's action is properly one for an "accounting."

In further reply to appellees' argument (Brief p. 107) permit us to respectfully state that we are not seeking an accounting for any sums of money or to replace any losses except *those of the Transamerica Corporation.* Where the Transamerica Corporation, as the real party in interest, is wronged it necessarily follows that its departments and agencies are harmed but this does not mean an "independent" harm, it is merely the manner of stating that the entire organization has suffered.

The decision in *Philipbar v. Derby,* 85 Fed. (2d) 27, mentioned by appellees (Brief pp. 108, 109, 110) does not involve a factual nor a legal situation as here presented except it is a stockholder's derivative suit against directors

for an *accounting* wherein the corporation was quite properly held to be an indispensable party. Appellees have gone far in an attempt to separate and have the "individual entities" of the several departments and agencies of the Transamerica Corporation considered as "parties in interest" in face of the admitted averments of the pleading.

The fact that the pleading alleges that the subsidiary departments and agencies suffered injuries and detriment in no manner changes the legal effect or sufficiency of the pleading as the Transamerica Corporation is also alleged to have *suffered the same injuries and detriment.* The expression noted, upon which appellees comment (Brief p. 111), is undoubtedly unnecessary to appellant's pleading but it is not fatal.

We are standing in this case upon the injury and detriment caused to the Transamerica Corporation by the manipulation of its funds and assets through and by means of its various agencies and departments. A fair interpretation of appellant's pleading so discloses. In support of our presentation of this subject in our opening brief we respectfully refer the court to the following cases:

Nichols & Co. v. Secretary of Agriculture, 131 Fed. (2d) 651, 7th Syl. Op. pp. 655, 656;

In re Otsego Wax Paper Co., 14 Fed. Supp. 15, 2d Syl., Op. p. 16;

In re Kentucky Wagon Mfg. Co., 71 Fed. (2d) 802, 2d Syl., Op. p. 804.

Replying to Appellee's Argument No. V.

(Brief pp. 113 to 129.)

Appellees' argument, in the respect here considered, is that by reason of conclusions of law set forth in appellant's pleading it is too vague, general and indefinite to state a claim.

At the outset it is well to note that in the argument in support of such contention as well as under appellees' points III and IV, reference is made to an argument based upon the appellees' motions for a more definite statement which were not decided by the trial court. This argument is brought forward in their discussion regarding the motions to dismiss because the trial court in its memorandum of conclusions made, as a reason for its decision ,a general conclusion which is far more vague and uncertain than appellant's pleading. This general and uncertain conclusion of the court, which we discuss under part I of our opening brief(pp. 45 to 68), appellees attempt to make definite by claiming that certain language in the pleading consists of conclusions of law and all that as so claimed relates to the allegations that the salary agreement and the credit entries which were used to perpetrate the fraud were "pretended, fraud and fictitious and that the credit entries were computed and unrealized profits." The later allegation is obviously one of ultimate fact. The former averment might be considered a conclusion but not when used in conjunction with the context of the entire paragraph wherein it is used. The salary agreement was pretended, fraudulent and fictitious because it was *definitely used for a wrongful purpose.* All of this is clearly charged and even the appellees do not contend that they could not prepare a responsive pleading thereto.

It is also claimed that the pleading is improper because it alleges that the appellees committed the corporate acts "without legal right or authority." Here again it is a debatable and doubtful statement to say that such an allegation as used in the pleading constitutes a conclusion of law or of the pleader. Whether one, under the circumstances averred, had a legal right or authority to perform an act for another must be factual.

A careful reading of appellees' argument discloses that with the exception of the case of *Swan v. Consolidated Water Co.,* 28 Fed. (2d) 971, decided in 1928, long prior to the effective date of the Federal Rules of Civil Procedure, the only decisions mentioned in support of appellees' argument come from California and other states not affected by the reformed practice. It certainly requires no argument to be assured that neither the common law or statutory rule of pleading of the states involved in such decisions bear any relationship to the rules now in effect in the Federal courts. In preparing the pleading in the present action we relied upon these rules and the decisions mentioned in our opening brief.

A considerable portion of appellees' argument is devoted to the Rule (9b), which requires the circumstances constituting fraud to be stated with particularity.

Neither the trial court's conclusion nor appellees' argument in any manner alter the plain and simple allegations of the pleading. Each and every wrongful or fraudulent act is stated with particularity and the only matter lacking

in the pleadings is the evidence showing the means used to perpetrate the wrongs. It is true, as argued by appellees (Brief p. 125), that fraud is never presumed, but, be that as it may, we submit that if the appellees did the things charged in the pleading they were guilty of frauds and civil wrongs. Here again it may be observed that we are not presently trying the case upon the merits nor presenting it upon evidence but on the other hand are submitting our case upon admitted allegations of a pleading permitted by a reformed procedure which should not be ignored in considering its sufficiency. We feel the situation justifies the following question: What material particularity is missing from appellant's pleading which makes it insufficient for a responsive pleading?

Neither the trial court nor opposing counsel have made an answer to this question. The details of that which appellees desire or may need to prepare for trial can readily be obtained by deposition and discovery.

Under this argument appellees, at pages 126, 127, 128 and 129 of their brief, again assume that appellant's action, instead of being one to *declare a trust and for a general accounting* to consist of several claims or causes of action. It seems that in practically all of appellees' several arguments recourse is made to this misapprehension of appellant's action and used as a basis for a discussion which evades the realities of the case. We again urge that appellant's pleading is sufficient within the meaning of the rules and the decisions cited in our opening brief and in further support thereof we refer to the following cases.

Relating to Point VI of Appellees' Brief Wherein an Attempt Is Made to Evade the Trial Court's Consideration of Evidence in Passing Upon Appellees' Motion to Dismiss.

(Appellees' Brief pp. 129-133).

At the outset it must be considered that appellees' motion to dismiss was the only one decided by the trial court. The appellees by correspondence with the Judge of the Court submitted photostatic copies of the minutes of the Board of Directors of the Transamerica Corporation relating to their meeting of December 9, 1931, and also two affidavits were presented one of Hector Campana [R. 271-273], and one of Edmund Nelson, Esq. [R. 269, 270.]

These documents, the effect of which appellees seek to evade by referring to them as material to the grounds of other motions not decided, are in fact material only for one purpose and that is with respect to the possibility of appellant receiving notice in 1931 of wrongdoing on the part of the Gianninis. These documents were *received by the court and filed.* They were not returned to the attorneys who transmitted the same.

It would indeed be destructive of legal philosophy to say that they were not considered by the trial court in passing upon the motions to dismiss in the face of the "conclusion" of the court contained in its Memorandum, namely [Tr. p. 492; Appellant's Br., Point II, pp. 36, 37]:

> "If the bar of the Statute of Limitations or of laches is to be avoided it will be necessary for plaintiff to plead other facts besides those set forth in her second amended complaint."

Appellees' argument that these documents are material in behalf of their motions for a separate statement of claims or to support the ground that the second amended complaint is a sham, is so far afield that some other explanation is due the court. It is quite obvious that these documents were considered because they were field and the point determined adversely to appellant.

The authorities upon this subject set forth in appellant's opening brief are indeed sufficient to require a reversal of the trial court's order and judgment and appellees have made no reply thereto.

The case of *Hewitt v. Great Northern Beet Sugar Co.*, 230 Fed. 394, mentioned at pages 132-133 of appellees' brief, has no relevancy to nor does it answer the discussion contained in our opening brief upon this subject.

Concerning the Bacigalupi letter of December 9, 1931, appellees now make the claim:

> "At least as far as these appellees were concerned the letter constituted an effective 'withdrawal' from the alleged conspiracy, even within the strict rule of criminal conspiracies stated in Eldredge v. U. S., 62 Fed. (2d) 449, 459, quoted in appellant's brief, page 105."

The appellant's pleading charges these very appellees with a *continuing* conspiracy and if the letter constitutes a "withdrawal" therefrom on the part of any appellee, then again the trial court considered evidence to unseat plain admitted facts.

Relating to Appellees' Supplemental Brief.

In this brief, the appellee, Bank of America National Trust and Savings Association, as Administrator of the Estate of John M. Grant, deceased, presents the point that appellant's claim is one "arising upon contract" and therefore must be dismissed because, prior thereto, it had not been presented to the administrator as required by Section 707 of the California Probate Code.

It is clear that if the foregoing provision of the California Probate Code is applicable, then the claims contemplated thereby must arise upon contract.

Counsel for this particular appellee, in their effect to sustain such a contention, cite at page 4 of the brief the following cases:

Norse v. Steele, 149 Cal. 303, 86 Pac. 693;

De Leonis v. Etchepare, 120 Cal. 407, 52 Pac. 718;

Allsop v. Joshua Hendy Machine Works, 5 Cal. App. 228, 90 Pac. 39;

Garcelon v. Commercial Travelers Ass'n, 184 Mass. 8, 67 N. E. 868.

The case of *Morse v. Steele,* 149 Cal. 303, is one where the defendant received from the plaintiff certain animals under an *express contract* that he would take care of them and on certain conditions return them to the plaintiff. He breached his contract and was therefore sued. We see no comparable likeness between this statement of facts and the situation presented in appellant's pleading in the present action.

In *De Leonis v. Etcheparc,* 120 Cal. 407, there was indeed an *implied contract* to account for the money belonging to the principal which the agent received.

In *Allsop v. Joshua Hendy Machine Works,* 5 Cal. App. 228, the action was fundamentally one upon an *implied contract.* One can always waive a tort upon such conditions and sue upon an implied contract.

In the case of *Garcelon v. Commercial Travelers Ass'n.,* 184 Mass. 8, the action was based upon a *contract* between the plaintiff and defendant irrespective of the alleged bad faith and fraudulent purpose of the defendant in refusing to comply therewith.

We do not feel called upon to make a detailed argument upon this point and in lieu thereof we respectfully refer the court to the following decisions:

Smith v. Smith, (9th Cir.)-224 Fed. 1, 3rd Syl., Op. p. 4;

Johnston v. McCluney, 80 S. W. (2d) 898, 8th Syl., Op. p. 93;

Leverone v. Weakly, 155 Cal. 395, 10th Syl., Op. p. 401;

Hardin v. Sin Claire, 115 Cal. 460, 2nd Syl., Op. pp. 463, 464;

Thompson v. Byers, 116 Cal. App. 214, 4th Syl., Op. p. 218.

Conclusion.

We have, by this brief, made an attempt to be useful to the Court and the matter stated is our sincere expression of the nature of appellant's case as interpreted by the laws and the rules of procedure applicable thereto.

As counsel for appellees have placed emphasis and reliance upon the contention that the "pleading" contains several claims, we again, at the risk of repetition, direct attention to the fact that the case is one to *establish a trust and compel the trustees to account.* It is but a single claim.

We also stand upon the proposition that the application of the "doctrine of laches" is factual and that *each case is a law unto itself* and, in that respect, we submit that there is nothing contained in appellant's pleading which directly or indirectly shows a lack of diligence on her part.

A pleading such as the one here involved is difficult to prepare from the viewpoint of one from whom material facts have been concealed but it is easy to criticize any pleading and we make no claim of perfection. However, we do submit that the "pleading" is sufficiently plain for a responsive pleading and that whatever so-called conclusions of law or of the pleader may be contained therein are not fatal to appellant's action.

Practically all of the matters urged by the appellees are points more properly directed to "discovery or pre-trial procedure."

For the reasons herein stated and those contained in our opening brief, we respectfully request that the order and judgment of the trial court be reversed and that we have our costs herein.

Respectfully submitted,

VINCENT A. MARCO,
PERCY V. CLIBBORN,
HOMER N. BOARDMAN,
Attorneys for Appellant.

APPENDIX.

(Excerpts from *Whitten v. Dabney,* 171 Cal. 621, Opinion p. 627):

> "This sufficiency indicates the gravamen of the charges of wrongdoing as they affect the corporation, and it certainly needs no discussion to establish that they charge sufficient facts to demand an investigation and inquiry by the court of equity to which the appeal has been made. So true and so apparent do we think this is, that we conclude that the court sustained the demurrer upon the ground that the statute of limitations was well pleaded, and to this proposition we next come."

(Opinion pp. 629, 630):

> "Respondents argue that from this pleading it is shown that the stockholder's alarms were excited; that they instituted inquiry and were thus put upon notice in 1906, and that this action not having been commenced until 1910, they have waited too long and relief must be denied. This contention demands again a brief consideration of this peculiar character of action. A stockholder who institutes it sues purely as a trustee to redress corporate injuries. *He has the unquestioned right to sue, but it is in no sense his duty to sue.* An individual stockholder may be put upon notice that his corporation has been defrauded. Indeed complete disclosure of these facts may be made to him. He gives consideration to the time, trouble, and expense of the litigation and the loss in which he would be involved if he failed to prevail, and decides that he will not begin the suit. Some years afterward another stockholder for the *first time* gains knowledge of these same facts and

institutes the action. It is susceptible of demonstration that the first stockholder knew of all these matters and that as to him this right of action may be bared. Is this also a bar to the prosecution of the same acion by another stockholder who has acted promptly upon learning of the fraud. *Clearly this cannot be so.* So long as the corporation itself remains under disability and powerless to act by virtue of the fact *that its* CONTROL *is in the hands of a board of directors accused of participation in the frauds* the statute of limitations does not run against it. It is like the minority of an infant. His rights are not lost until, he after attaining majority, acquiesces for the prescribed time and by acquiescence affirms the acts done against his interests. So that even if it be said (and in saying it we do not decide it) that such a complaint as this shows that the plaintiff stockholder has waited too long before commencing his action, and that therefore the plea of the statute of limitations must be sustained against his action, *this does not operate as a bar to the corporate rights when prosecuted by another stockholder.* Otherwise we would have the anomalous and absurd condition presented of a complacent stockholder waiting for three years, pleading facts showing that his right of action was thus barred, and thus sweeping away every right of the corporation by the judgment which would have to follow. Whatever, therefore, may have been the rights of the Providence stockholders to prosecute this after notice, *the right of these plaintiffs is not* barred under the allegation that they first acquired notice and knowledge of the efforts of the Providence stockholders in 1910."

(Excerpt from *Baillie v. Columbia Gold Mining Co.*, 86 Ore. 1, Opinion p. 15):

> "Error is assigned on the order of the Circuit Court overruling the demurrer to the amended complaint. The demurrer charges multifariousness, insufficiency of facts and failure to bring the suit within the time limited by the Oregon Code. We do not think the complaint multifarious. It alleges a series of fraudulent acts committed by the defense by virtue of their control of the defendant Columbia Gold Mining Company, hereinafter called the Columbia Company. The allegations with reference to plaintiff's right to injunction are properly pleaded in a single count with other allegations. Our conclusions on the branch of the case are in harmony with those of the Federal Court;
>
> Baillie v. Backus, 230 Fed. 711, 716."

(Excerpt from *Van Schaick v. Aron*, 10 N. Y. Supplement (2d) 550, Opinion pp. 561, 562):

> "Whatever the law may have been therefore, it is clear that the knowledge of wrongdoing directors, in the light of the discovery provision, may not be imputable to the corporation so as to commence the running of the limitation period. To so determine would render the discovery provision nugatory, for otherwise, in every case, the statute would of necessity begin to run from the date of the transaction. The decision in other jurisdictions based on substantially similar statutory provisions are to this effect and no decisions to the contrary have been presented to the court.
>
> Smith v. Lyle, 59 S. D. 534, 241 N. W. 512;
>
> Adams v. Clarke, 9 Cir., 22 F. (2d) 957;
>
> Reid v. Robinson, 64 Cal. App. 46, 220 P. 676.

It is untenable to assume that wrongdoing directors would set in motion proceedings to charge themselves with liability because of their illegal acts. In an unreported decision the late Mr. Justice Tierney stated: 'Under this statute, however, it would be unreasonable to hold that acts of misconduct of an officer or director were discovered by the corporation because an officer or director knew of them. In such a case, two offending officers or directors could give one another absolution by keeping silent as to the other's derelictions.'

Phillips v. Bank of New York.

In the instant case the wrongdoing directors were in exclusive control of the affairs of the corporation up to March 9, 1932. The basis of their liability, whether for negligence or for active participation in the wrongful acts, is not significant, the statute is tolled so long as the controlling directors are subject to suit and liability for their acts. Of course the knowledge of the new directors who were elected on March 9, 1932 is imputable to the corporation but that date is less than three years from the date of actual suit. The statute of limitations becomes operative as of that date."

(Excerpts from *Reid v. Robinson,* 64 Cal. App. 46, Opinion pp. 48, 55, 56):

"This action sounds in fraud. It is brought by certain persons who, during a portion of the time involved herein, were stockholders of a corporation. The purpose of the action is to compel certain other persons, who were likewise stockholders and directors of the corporation, to account for alleged secret profits made by one of them in which he was

aided and abetted by the other of them (although not to his profit) in the sale of certain real property belonging to the corporation.

It is earnestly contended that Reid at least, being a director of the land company, had means of knowledge and that the circumstances were such as to place him on inquiry to the end that he must have had notice of the fraud at so early a date in connection with the transaction in question as would start the operation of the statute and bar the action before suit was commenced. It is true that the minutes of the corporation do disclose such acts and inferences as, assuming that Reid actually read them, should have placed him as a prudent man on inquiry. He denied that he ever read the minutes until at a time very shortly before the suit was commenced. There was other evidence, both for and against, as far as notice to Reid was concerned, but very little, if any, to show notice on the part of the other plaintiffs. The evidence was conflicting and the determination of the truth rested finally with the trial court."

(Opinion p. 56):

"There was no duty or obligation encumbent upon either Reid or any of his co-plaintiffs to examine the books or the minutes of the corporation either constantly or at intervals for the purpose of detecting fraudulent acts or transactions either as against the stockholders generally or as against themselves in particular. The case of Prewitt v. Sunnymead Orchard Co., 189 Cal. 723 (209 Pac. 995), contains the declaration of law that 'inasmuch as respondents had no actual knowledge of circumstances which would lead her to examine the books or the matters

which appeared therein, and as there was no duty imposed on her by law to examine them, she cannot be charged with constructive knowledge of the facts which an examination of the books might have led her to discover.' The same principal of law is announced in Pacific Vinegar Works v. Smith, 152 Cal. 507 (93 Pac. 85), and the following cases are also in point. First National Bank v. Drake, 29 Kan. 311 (44 Am. Rep. 646); Rudd v. Robinson, 126 N. Y. 113 (22 Am. St. Rep. 816, 12 L. R. A. 463, 26 N. E. 1046)."

(Excerpts from *Fleishhacker v. Bloom,* 109 Fed. (2d) 543, Opinion p. 548):

"The pleadings did not specifically frame an issue in respect of the bank's notice or knowledge of the fraud. We doubt, therefore, that appellants are in a position to urge the bar of the statute in so far as it relates to the bank itself. Whether the trial court regarded the statute as having been waived by failure properly to plead it, and for that reason made no finding, we are unable to determine. However, since the parties have assumed that the question is properly before us, we will consider and decide it."

(Excerpt from *Dodge v. Woolsey,* 59 U. S. 331, 345):

"Now, in our view, the refusal upon the part of the directors, by their own showing, partakes more of disregard of duty, than of an error of judgment. *It was a non-performance of a confessed official obligation, amounting to what the law considers a*

breach of trust, though it may not involve intentional moral delinquency. It was a mistake, it is true, of what their duty required from them, according to their own sense of it, but, being a duty by their own confession, *their refusal was an act outside of the obligation which the charter imposed upon them to protect what they conscientiously believed to be the franchises of the bank. A sense of duty and conduct contrary to it, is not 'an error of judgment merely,'* and cannot be so called in any case. *It amounted to an illegal application of the profits due to the stockholders of the bank,* into which a court of equity will inquire to prevent its being made."

(Excerpt from *Stone v. Winn,* 165 Kentucky 9, Opinion pp. 30, 31):

"Aside from the construction of the Enabling Act of 1888, and the proposition submitting the question to a vote, this entire case is based upon the allegation of fraud in the election in which the proposition to make the subscription on behalf of the country was carried. In addition to the plea of *res judicata* the appellants interposed a plea of limitation to this action, based upon Section 2519 of the Kentucky Statute, which provides that in actions for relief for fraud or mistake, the cause of action shall not be deemed to have accrued until after the discovery of the fraud or the mistake, but that no such action shall be brought ten years after the time of making the contract, or the per-

petration of the fraud. As this allegation was held on August 11, 1888, and this action was not brought until June 18, 1913, nearly twenty-five years thereafter, it is clearly barred by limitation.

Moreover in the case filed by Estell County against the Railway Company in the Estell Common Pleas Court in 1891, as above pointed out in this opinion, the ground upon which the county sought to stop the delivery of the bonds was fraud perpetrated in the election of 1888.

Under the statute above quoted the time of the discovery of the fraud can have no bearing upon this case since more than ten years have elapsed since the perpetration of the alleged fraud."